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SUBJECT: NEW LATVIAN GAS STORAGE UNLIKELY WITHOUT PUSH FROM
NEIGHBORS

¶1. (SBU) Summary: Latvia is entirely dependent on Russia for natural gas supplies. Increased natural gas storage capacity could act as a stronger buffer against a potential cutoff - but prospects for a commercial project are bleak. While there has been some discussion of a new storage facility, Latvijas Gaze holds a monopoly on gas transit in the country, and sees no commercial potential for such a project. Only significant outside efforts, such as funding from the EU, would make such a project realistic in the medium-term.

Existing and proposed capacity

¶2. (U) The storage facility at Incukalns holds 4.5 billion cubic meters (bcm) of gas, with 2.3 bcm active and the rest serving as a necessary "cushion." Officials at Incukalns say they could expand capacity to 5.5 bcm without significant investment and to 6.2 bcm (3.2 bcm active) with only modest investment. The most frequently mentioned potential new storage site is Dobeles, a structure in southwest Latvia that could potentially hold 20 bcm (10 bcm active). Existing Soviet-era studies of Dobeles's suitability give it a cost advantage over other sites. There are, however, other large structures suitable for gas storage that are much closer to the coast, making them more suitable for LNG or pipeline connections.

¶3. (U) After having dropped from sight, discussion of the topic has increased in recent months. The most prominent reason was Gazprom's new representative office in Latvia. During a television news segment on the new office, Gazprom representative Jevgenijs Roldugins discussed at some length the potential to build additional storage that could be connected to NordStream. He claimed that Gazprom is ready to move ahead on a storage project, but that delays were due to the European side.

Limited commercial interest in Dobeles

¶4. (SBU) NordStream Baltic representative Romans Baumanis says that there is no chance now of NordStream working to connect to Latvia. He stated that a new storage facility is simply not commercially viable. While the infrastructure costs of a new storage facility are substantial, the real barrier is the 10 bcm of cushion gas, the cost of which could not be offset by the revenue generated by storage fees.

¶5. (U) Latvijas Gaze (LG) officials argue that the existing Incukalns facility is sufficient to meet all of the Baltic States' needs, and therefore investment in a new facility could only be feasible if it had customers from elsewhere in Europe. They are considering plans to expand Incukalns to take advantage of a potential pipeline connection to Finland, but absent such a new market, the current capacity is sufficient to meet demand for storage. LG (majority owned by Gazprom and its associates) holds monopoly contracts on all existing gas transit lines in Latvia. Constructing storage capacity would not get Latvia around the monopoly on distribution.

¶6. (SBU) Some independent analysts see greater potential. Gregory Rubinchik (protect), a Senior Manager at KPMG focused on the energy

industry, argues that project detractors are ignoring the potential profit in speculation on energy prices. While certainly a riskier proposition, a company with the cash to invest up front could fill a storage facility while prices are low and sell when prices rise - and given projected long-term trends on energy prices, storage facilities could be hugely profitable. He further argues that Gazprom and others interested in the status quo dominate the issue and prevent serious discussion.

Existing contracts and GOL opinions

¶7. (U) The new EU Baltic Energy Market Interconnection Plan (BEMIP) notes that better gas grid connections in the region could open the potential for increased gas storage in Latvia, but the GOL does not see the urgency. The government cites factors ameliorating their dependency on Russian sources, and notes that the GOL could not finance additional strategic capacity themselves even if the need existed. Government sources argue that because gas from the existing storage facility is pumped back to Russia to heat St. Petersburg in the winter, any attempt by Russia to cut off Latvia from gas would be self-defeating. (FYI: Incukalns holds enough gas to heat all of Latvia for at least one and, possibly, two years.) The GOL argues that if cut off, they would nationalize the gas, freezing St. Petersburg in the process. It is likely, however, that any such attempt by Latvia would be fraught with legal and political peril.

¶8. (SBU) Comment: Gas storage in Latvia could still be a part of a plan to increase gas security overall, but it will need to be based on demand from outside of Latvia. The GOL does not feel enough urgency to prioritize new storage given the many fiscal challenges facing the country. If Latvian storage is going to be part of a broader European security strategy, the driver will likely have to be the storage customers in neighboring countries, not the potential storage providers here.

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